

**CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM  
HYBRID INVESTMENTS MONITORING REPORT**

**Relational Investors**

Third Quarter 2005

**Investment Type:** U.S. Corporate Governance Fund

**Inception Date:** March 1996

**Capital Commitment:** \$750 million

	<u><b>Quarter</b></u>	<u><b>Since Inception</b></u>
<b>Contributed Capital:</b>	\$ 70.3 million	\$2,566.4 million
<b>Distributed Capital:</b>	\$ 34.9 million	\$2,105.7 million

**Market Value (9/30/05):** \$ 1,192.7 million

**Investment Strategy:**

Relational Investors employs a corporate governance strategy aimed at unlocking intrinsic value in underperforming, publicly traded, U.S. companies. When compared to the broader market and industry peers, these companies typically exhibit inferior performance in one or more of the following areas: operations, financial structure, long-term strategy, corporate governance policies or management. Each investment represents a significant percentage of a particular company's outstanding shares, generally 3-10%. Relational Investors then seeks to maximize investment value by initiating contact with the company's management, board of directors and other shareholders to facilitate change.

**Summary Analysis:**

***Number of Investments: 13***

Organization: Relational has closed to new investors as assets under management have reached \$6.0 billion.

Philosophy/Process: No material changes.

**Performance Analysis:**

Since inception through September 30, 2005, Relational has outperformed its benchmark by 17.57% on an annualized basis.

	<b>Since Inception</b>
Relational Investors (IRR)	25.53%
S&P 500 Index (IRR)	7.96%
Excess Return	17.57%

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**Active Value**  
Third Quarter 2005

**Investment Type:** European Corporate Governance Fund

**Inception Date:** September 1998

**Capital Commitment:** \$350 million

	<u><b>Quarter</b></u>	<u><b>Since Inception</b></u>
<b>Contributed Capital:</b>	\$ 0.1 million	\$ 354.5 million
<b>Distributed Capital:</b>	\$ 18.7 million	\$ 325.8 million

**Market Value (9/30/05):** \$ 117.7 million

**Investment Strategy:**

Active Value Capital employs a corporate governance strategy aimed at unlocking intrinsic value in under performing, publicly traded, European companies. Active Value Capital targets fundamentally strong companies with leading positions in their respective industries that suffer from poor management, have a capital structure in need of restructuring, have undervalued brands or franchises, suffer from over-expansion or are in industries likely to undergo consolidation. Each investment will consist of either 25% of a company's outstanding preference shares or 10% of a company's ordinary shares where preference shares do not exist. Active Value then seeks to maximize investment value by initiating contact with the company's management, board of directors and other shareholders to facilitate change.

**Summary Analysis:**

***Number of Investments: 5***

Organization: Active Value has indicated that the portfolio is likely to complete liquidation and returned to investors during the first half of 2006.

Philosophy/Process: No material changes.

**Performance Analysis:**

Since inception through September 30, 2005, Active Value's Total Composite, which is comprised of Class A, Class CIP and Pledge A, underperformed its benchmark by 0.30% on an annualized basis. The Class A & CIP Composite underperformed by 0.76%, while Pledge A outperformed by 0.67% on an annualized basis.

<b>Since Inception</b>	<b>Total Composite</b>	<b>Class A &amp; CIP Composite</b>	<b>Pledge A</b>
Active Value (IRR)	7.28%	6.81%	8.27%
FTSE 250 Index (IRR)	7.58%	7.57%	7.60%
Excess Return	-0.30%	-0.76%	0.67%

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**Hermes Lens**  
Third Quarter 2005

**Investment Type:** U.K. Corporate Governance Fund

**Inception Date:** November 1999

**Capital Commitment:** \$200 million

	<u><b>Quarter</b></u>	<u><b>Since Inception</b></u>
<b>Contributed Capital:</b>	\$ 0.0 million	\$ 199.9 million
<b>Distributed Capital:</b>	\$ 0.0 million	\$ 0.0 million

**Market Value (9/30/05):** \$ 295.6 million

**Investment Strategy:**

Hermes Lens Asset Management (HLAM) employs a corporate governance strategy that seeks to unlock intrinsic value in underperforming, medium-to-large capitalization, publicly traded, U.K. companies. For companies that meet their initial purchase criteria, HLAM identifies areas where value can be improved and recommends strategies for change to the board of directors and company executives. Proposed changes focus on the structure and composition of the board and management, strategic business plans and capital structure. HLAM initially expects to invest in 5-10 companies but intends to be invested in 15 companies as assets grow. Initial positions will range from 1-3% with open market purchases of common stock, however the goal is to have influence over 15-20% of a target company's outstanding shares. All cash balances will be equitized with FTSE 250 futures.

**Summary Analysis:**

***Number of Investments: 14***

Organization: No material changes.

Philosophy/Process: No material changes.

**Performance Analysis:**

Since inception through September 30, 2005, the Hermes UK Focus Fund has outperformed its benchmark by 3.86% on an annualized basis.

	<b>Since Inception</b>
Hermes UK (IRR)	6.88%
FTSE All Share (IRR)	3.02%
Excess Return	3.86%

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**SPARX Asset Management**  
Third Quarter 2005

**Investment Type:** Japanese Corporate Governance Fund

**Inception Date:** January 2003

**Capital Commitment:** \$200 million

	<u><b>Quarter</b></u>	<u><b>Since Inception</b></u>
<b>Contributed Capital:</b>	\$ 53.0 million	\$ 544.9 million
<b>Distributed Capital:</b>	\$ 12.9 million	\$ 214.6 million

**Market Value (9/30/05):** \$ 520.6 million

**Investment Strategy:**

The SPARX Value Creation Fund targets underperforming or undervalued companies based in Japan with a market capitalization between \$300 million and \$3 billion. The SPARX Research Platform, which is a research team of ten analysts, will use quantitative and qualitative screens to identify approximately 40 target companies from the SPARX database of 2,500 companies. The Value Creation group then will conduct in-depth research on these target companies by initiating contact with company management. These companies typically exhibit one or more of the following traits: low valuation, potential for balance sheet optimization, or potential for profit improvement. The fund looks to invest in 5-10 companies per year with 5-20% of net asset value dedicated to each investment. It will actively engage and work in partnership with management or major shareholders to unlock the investment's value over a specified period of time. The performance objective for the fund is the Topix Index + 150 basis points.

**Summary Analysis:**

***Number of Investments: 8***

**Organization:** The VCI team added two analysts during the quarter. Ningguo Yang transferred internally to the VCI team. Hiroshi Yamamoto is a newly hired analyst. Both are responsible for screening for potential investments and supporting managers with their engagements.

**Philosophy/Process:** No material changes.

**Performance Analysis:**

Since inception through September 30, 2005, SPARX has outperformed its benchmark by 11.48% on an annualized basis.

	<b>Since Inception</b>
SPARX Value Creation (IRR)	37.05%
Topix Index (IRR)	25.57%
Excess Return	11.48%

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**Hermes Lens**  
Third Quarter 2005

**Investment Type:** European Corporate Governance Fund

**Inception Date:** August 2003

**Capital Commitment:** \$100 million

	<u><b>Quarter</b></u>	<u><b>Since Inception</b></u>
<b>Contributed Capital:</b>	\$ 0.0 million	\$ 100.0 million
<b>Distributed Capital:</b>	\$ 0.0 million	\$ 0.0 million

**Market Value (9/30/05):** \$ 165.0 million

**Investment Strategy:**

Hermes Lens Asset Management (HLAM) employs a corporate governance strategy that seeks to unlock intrinsic value in underperforming, medium-to-large capitalization, publicly traded, European ex-U.K. companies. For companies that meet their initial purchase criteria, HLAM identifies areas where value can be improved and recommends strategies for change to the board of directors and company executives. Proposed changes focus on the structure and composition of the board and management, strategic business plans and capital structure. HLAM initially expects to invest in 5-10 companies but intends to be invested in 15 companies as assets grow. Initial positions will range from 1-3% with open market purchases of common stock, however the goal is to have influence over 15-20% of a target company's outstanding shares. All cash balances will be equitized with FTSE Europe ex-U.K. futures.

**Summary Analysis:**

***Number of Investments: 18***

Organization: Hermes Europe added a new manager, Maarten Wildschut. Maarten spent the last seven years with Robeco Asset Management. Maarten will be replacing Paola Perotti and the two will be working together over the next several months to ensure a smooth transition.

Philosophy/Process: No material changes.

**Performance Analysis:**

Since inception through September 30, 2005, the Hermes Europe Focus Fund has outperformed its benchmark by 2.61% on an annualized basis.

	<b>Since Inception</b>
Hermes Europe (IRR)	28.35%
FTSE Europe ex-U.K. (IRR)	25.74%
Excess Return	2.61%

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**Taiyo Pacific Partners/WL Ross**  
Third Quarter 2005

**Investment Type:** Japanese Corporate Governance Fund

**Inception Date:** July 2003

**Capital Commitment:** \$199.6 million

	<u>Quarter</u>	<u>Since Inception</u>
<b>Contributed Capital:</b>	\$ 4.8 million	\$ 299.5 million
<b>Distributed Capital:</b>	\$ 0.0 million	\$ 0.0 million

**Market Value (9/30/05):** \$ 443.4 million

**Investment Strategy:**

Taiyo Pacific Partners/WL Ross believe that public equity investors in Japan can be rewarded with superior returns by investing in companies that will implement corporate governance improvements. The investment strategy has two elements. First, identify undervalued stocks utilizing Taiyo's asset value and earnings potential analysis. Second, create valuation improvements by means of a three-phase corporate governance strategy. The three phases are: improving transparency and disclosure, improving corporate profitability, and improving shareholder value. Taiyo proposes to use its own proprietary database to identify target companies. Once identification is made, Taiyo's strategy is to be a constructive shareholder with those companies willing to make corporate governance improvements.

**Summary Analysis:**

***Number of Investments: 13***

**Organization:** Taiyo recently moved to a bigger office to accommodate its growing staff. The firm has been adding staff to develop its back office capabilities. It is planning to shift back office operations from WL Ross to its office in Monterey, CA. This is expected to happen in the first quarter of 2006.

**Philosophy/Process:** No material changes.

**Performance Analysis:**

Since inception through September 30, 2005, Taiyo has outperformed its benchmark by 11.77% on an annualized basis.

	<b>Since Inception</b>
Taiyo (IRR)	33.07%
Topix Index (IRR)	21.30%
Excess Return	11.77%

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**Knight Vinke**  
Third Quarter 2005

**Investment Type:** European Corporate Governance Fund

**Inception Date:** June 2003

**Capital Commitment:** \$200 million

	<u><b>Quarter</b></u>	<u><b>Since Inception</b></u>
<b>Contributed Capital:</b>	\$133.1 million	\$ 265.6 million
<b>Distributed Capital:</b>	\$ 11.2 million	\$ 85.5 million

**Market Value (9/30/05):** \$ 218.5 million

**Investment Strategy:**

Knight Vinke believes that in the absence of effective corporate governance and a truly independent board, the separation of ownership and management can create the opportunity for management to act in its own self interest rather than that of the shareholders. The strategy looks to identify underperforming stocks of companies that are fundamentally strong where redress of the underperformance is possible in a reasonable amount of time. The firm believes that detailed fundamental analysis can identify underperforming companies that have strong operating businesses, but are in need of a corporate finance solution to a factor or factors that specifically is depressing the share price. To identify such companies the firm uses several sources: its own screening process through market information services such as Bloomberg, their own industry knowledge, outside brokers, other institutional shareholders, other corporations, industry manager who may have recently retired, or corporate finance professionals.

**Summary Analysis:**

***Number of Investments: 5***

Organization: No material changes.

Philosophy/Process: No material changes.

**Performance Analysis:**

Since inception through September 30, 2005, Knight Vinke has outperformed its benchmark by 9.04% on an annualized basis.

	<b>Since Inception</b>
Knight Vinke (IRR)	29.15%
FTSE World Series Europe (IRR)	20.11%
Excess Return	9.04%

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**Shamrock Capital**  
Third Quarter 2005

**Investment Type:** U.S. Corporate Governance Fund

**Inception Date:** December 2004

**Capital Commitment:** \$100 million

	<u><b>Quarter</b></u>	<u><b>Since Inception</b></u>
<b>Contributed Capital:</b>	\$ 7.8 million	\$ 50.1 million
<b>Distributed Capital:</b>	\$ 0.0 million	\$ 0.0 million

**Market Value (9/30/05):** \$ 50.7 million

**Investment Strategy:**

Shamrock believes that combining a deep value investment orientation with an activist shareholder approach founded upon best governance practices, results in superior returns for long-term investors. They seek to find underperforming but fundamentally sound businesses, where they can substantially improve shareholder value with their application of good governance practice. They choose to look at companies they can purchase at a significant discount (<40%) to the underlying value and find free cash flow available to owners that typically exceed 10%. Once these criteria are met, Shamrock will only invest if they believe they can persuade the Board and/or management to believe in their activist strategy to make fundamental changes to the governance structure and business. After investing, persistence and careful monitoring is the key to unlocking value.

**Summary Analysis:**

***Number of Investments:*** 3

Organization: No material changes.

Philosophy/Process: No material changes.

**Performance Analysis:**

Since inception through September 30, 2005, Shamrock has underperformed its benchmark by 9.51%. However, the manager has had a short tenure so far. We expect performance to improve as the manager adds more holdings to the portfolio and as engagements with companies mature.

	<b>Since Inception</b>
Shamrock (IRR)	2.24%
Russell 2000 (IRR)	11.75%
Excess Return	-9.51%

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**Blum Capital**  
Third Quarter 2005

**Investment Type:** U.S. Corporate Governance Fund

**Inception Date:** July 2005

**Capital Commitment:** \$125 million

	<u><b>Quarter</b></u>	<u><b>Since Inception</b></u>
<b>Contributed Capital:</b>	\$ 34.0 million	\$ 34.0 million
<b>Distributed Capital:</b>	\$ 0.6 million	\$ 0.5 million

**Market Value (9/30/05):** \$ 33.0 million

**Investment Strategy:**

Blum believes that its private equity investment approach executed in the small- and mid-cap sectors of the public market results in superior returns for long-term investors. Blum seeks to find undervalued “good businesses”, where it can substantially improve shareholder value by working in partnership with management and Boards of Directors to implement value-enhancing strategies. Blum chooses to look at companies with a 10% cash-on-cash yield combined with a projected 10% growth rate in the free cash flow. Once the criteria are met, Blum will only invest if it believes that management and the Board will be receptive to its suggestions. The benchmark for Blum is an absolute return of 8% per annum.

**Summary Analysis:**

***Number of Investments: 13***

Organization: No material changes.

Philosophy/Process: No material changes.

**Performance Analysis:**

Blum does not have a full quarter of performance. Performance reporting will start next quarter.